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VIRGINIA BUSINESS REPORT

BUREAU OF BUSINESS RESEARCH, SCHOOL OF BUSINESS ADMINISTRATION
THE COLLEGE OF WILLIAM AND MARY, WILLIAMSBURG, VIRGINIA
Report No. 291 **August, 1984**

Business in Virginia July, 1984 Data

Virginia's business activity in July generally mirrored the national development, with slowing growth in the majority of the indicators we report. The notable exception was in the State's new car registrations, which were 28.6 percent higher in July 1984 than July 1983. The national year-over-year growth in new car sales for July was only 9.5 percent. Therefore, in July as well as June, Virginians' demand for new automobiles grew at a much more rapid pace than nationally. Plus, other evidence suggests that the growth in demand for other types of durable goods also grew significantly more in the Commonwealth than nationally. Our better employment situation, with continuing employment growth and an unemployment rate well below the U.S. rate, probably is the major reason. It not only produces more confidence in the future but also gives our consumers above-average financial capacity to satisfy the pent-up demand which developed in the four years from 1979 through 1982. Every time this year that we have thought the durable goods boom in Virginia finally was showing signs of winding down, consumers have turned around and gone on another buying spree, in spite of higher interest rates and tighter supplies. The durable goods growth will slow to more normal rates in the future, but we have decided to wait for very conclusive evidence before offering any more advice on **when** that will occur.

Chart I

Nine Selected Business & Economic Indicators Percentage Change

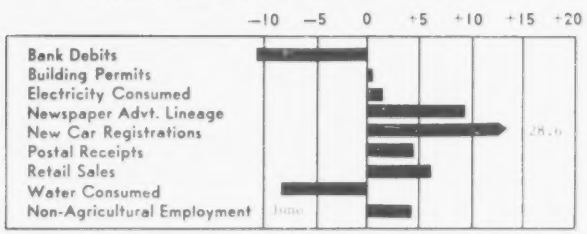
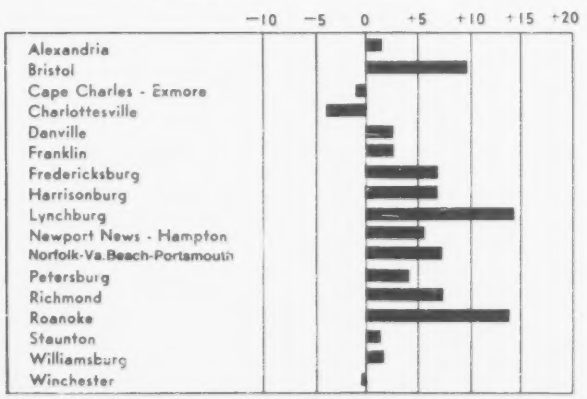


Chart II

City Indices



The most negative indicator for the State was water consumption, down almost everywhere. That result is easy to deal with--everyone will agree the July weather was the cause. So, in discussing the overall **economic** performance of the State and individual urban areas, we will omit consideration of water consumed.

Building permits Statewide did hold even with last July's exceptional performance. However, that resulted from high growth in five areas, offsetting a decline in the other 12 covered. The evidence indicates that the rising mortgage rates definitely are ending the building boom in most parts of the Commonwealth. Aside from construction, and a mild decline in tourism in some parts of the State, the general pattern is economic activity still is either growing or at least remaining steady at a high level. Thus Virginia's business outlook still remains very favorable.

The individual urban areas did reveal quite diverse movements, so some brief comments on each area are appropriate. In the **Alexandria-Northern Virginia area,** building permits grew at a more rapid pace, and employment growth still is well above the State average. However, the pace of growth in both durable and non-durable retail sales seems to have slowed quite dramatically.

The **Bristol, Virginia area,** which we noted in the back-page article last month was improving dramatically, still is growing strongly. Building permit growth remains exceptionally high, the employment growth for June rose compared to May and was the highest among the metropolitan areas we report, plus retail sales growth in July was about

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SELECTED BUSINESS AND ECONOMIC INDICATORS
FOR 17 CITIES

TABLE I JULY, 1984

Monthly Index Number Comparisons of Current Month to Same Month in Base Period (1977 = 100)

CITY	CITY INDEX *	BANK DEBITS *	BUILDING PERMITS	ELECTRICITY CONSUMED	NEWS-PAPER ADV. LINAGE	NEW CAR REGIS-TRATIONS	JUNE NON AGRI-CULTURAL EMPLOYMENT #	WATER CONSUMED	RETAIL SALES †	POSTAL RECEIPTS
The State		300.4	181.1	136.7	95.8	126.6	118.1	93.9	149.7	244.6
Alexandria	125.6	259.4	858.3	142.8	N.A.	131.0	123.9	104.6	125.8	N.A.
Bristol	128.2	230.2	92.0	83.0	68.6	104.2	N.A.	96.6	143.2	143.4
Cape Charles - Exmore	119.6	269.1	272.1	123.8	N.A.	97.1	N.A.	N.A.	110.0	166.5
Charlottesville	169.0	349.8	163.9	126.4	N.A.	126.4	N.A.	117.6	193.3	232.6
Danville	133.7	N.A.	150.9	116.5	98.8	96.0	N.A.	85.2	148.4	226.2
Franklin	124.6	N.A.	32.9	116.3	95.1	123.7	N.A.	111.7	115.9	202.2
Fredericksburg	174.1	79.9	128.7	N.A.	131.0	160.4	N.A.	62.9	170.3	353.6
Harrisonburg	138.4	259.4	216.7	N.A.	128.3	91.6	N.A.	124.0	139.0	207.6
Lynchburg	176.4	595.0	101.1	113.7	N.A.	104.9	N.A.	126.1	161.9	404.7
Newport News - Hampton	123.2	207.5	223.1	127.9	72.6	86.8	123.0	118.2	152.4	N.A.
Norfolk - Va. Beach - Portsmouth	148.2	285.9	218.9	157.7	118.9	100.7	140.4	85.5	194.1	N.A.
Petersburg	104.0	108.4	611.6	N.A.	51.5	87.0	N.A.	96.0	104.8	178.9
Richmond	133.8	332.4	N.A.	151.2	106.9	119.3	113.9	107.8	126.1	226.5
Roanoke	137.9	255.0	223.3	102.3	127.5	83.5	109.5	102.3	155.4	249.8
Staunton	117.7	162.0	45.7	N.A.	82.7	95.5	N.A.	N.A.	115.3	182.3
Williamsburg	143.4	174.7	253.8	175.2	N.A.	114.0	N.A.	108.2	116.3	257.3
Winchester	131.1	364.6	49.9	118.8	157.8	126.3	N.A.	121.2	90.1	254.0

TABLE II July, 1984

Percentage Change from same month last year

CITY	CITY INDEX *	BANK DEBITS*	BUILDING PERMITS	ELECTRICITY CONSUMED	NEWS-PAPER ADV LINAGE	NEW CAR REGIS-TRATIONS	JUNE NON AGRI-CULTURAL EMPLOYMENT#	WATER CONSUMED	RETAIL SALES †	JUNE RETAIL SALES ‡
The State		-10.5	0.5	1.6	9.6	28.6	3.7	-8.5	5.8	26.9
Alexandria	1.4	40.2	64.0	-4.4	N.A.	5.4	5.6	-1.1	1.4	24.7
Bristol	9.7	6.3	170.3	-0.5	-2.6	38.7	5.7	3.0	11.1	32.4
Cape Charles - Exmore	-0.6	66.5	-56.5	0.3	N.A.	39.5	N.A.	N.A.	-14.3	9.5
Charlottesville	-4.2	14.7	-41.1	2.6	N.A.	-2.0	-0.7	-6.1	-7.8	44.0
Danville	2.2	N.A.	-65.1	-5.2	5.3	0.7	1.3	-0.2	5.1	18.5
Franklin	2.2	N.A.	-81.9	-0.6	-2.7	21.0	N.A.	-10.1	2.7	15.5
Fredericksburg	6.6	-13.9	-13.1	N.A.	5.6	43.4	N.A.	-10.4	0.3	36.7
Harrisonburg	6.6	45.3	-13.3	N.A.	14.8	1.8	N.A.	4.7	6.0	27.8
Lynchburg	14.3	37.1	-23.6	5.5	N.A.	3.0	3.9	8.8	26.4	36.3
Newport News - Hampton	5.3	23.4	71.8	5.9	9.9	22.6	4.9	-16.8	5.3	18.0
Norfolk - Va. Beach - Portsmouth	6.9	-25.8	-18.6	5.6	14.5	14.1	5.3	-3.6	6.3	28.0
Petersburg	3.7	33.3	560.0	N.A.	-10.4	53.3	-1.7	-18.2	1.0	30.2
Richmond	7.2	-9.1	-8.4	1.3	14.6	42.9	2.2	-15.2	3.9	35.4
Roanoke	14.0	-3.6	-4.9	18.9	8.7	31.6	2.6	-11.1	20.4	39.8
Staunton	0.8	26.9	-50.4	N.A.	6.0	20.3	N.A.	N.A.	-7.4	12.1
Williamsburg	1.4	82.7	54.8	5.3	N.A.	-2.9	N.A.	0.6	1.7	22.1
Winchester	-0.1	20.7	-24.6	7.6	6.1	13.2	N.A.	0.6	-9.3	47.6

TABLE III

Percentage Change January - July from same period last year

CITY	CITY INDEX*	BANK DEBITS*	BUILDING PERMITS	ELECTRICITY CONSUMED	NEWS-PAPER ADV LINAGE	NEW CAR REGIS-TRATIONS	JAN. - JUNE NON AGRI-CULTURAL EMPLOYMENT #	WATER CONSUMED	RETAIL SALES †	JAN. - JUNE RETAIL SALES ‡
The State		5.8	23.6	9.2	11.7	20.3	3.7	4.4	7.9	24.8
Alexandria	8.6	32.4	16.4	5.5	N.A.	16.9	5.6	2.8	9.8	27.5
Bristol	17.3	-5.6	141.3	9.8	-1.0	28.1	5.7	21.9	24.7	24.2
Cape Charles - Exmore	0.8	-33.4	-44.2	-3.6	N.A.	35.0	N.A.	N.A.	-9.2	15.8
Charlottesville	1.2	30.0	136.4	9.7	N.A.	13.8	-0.7	-4.4	-3.3	28.5
Danville	7.0	N.A.	107.9	3.9	10.3	21.3	1.3	3.8	5.0	22.3
Franklin	8.9	N.A.	-30.2	8.0	4.6	33.1	N.A.	-5.1	7.3	22.6
Fredericksburg	13.5	7.3	-7.7	N.A.	8.2	37.9	N.A.	3.2	10.6	48.2
Harrisonburg	10.4	33.6	84.3	N.A.	11.8	11.0	N.A.	6.4	11.0	33.6
Lynchburg	11.7	-18.6	-14.8	7.7	N.A.	19.0	3.9	11.3	13.3	27.0
Newport News - Hampton	6.6	11.6	47.4	9.7	13.1	21.2	4.9	0.4	1.2	18.5
Norfolk - Va. Beach - Portsmouth	10.5	9.5	16.7	10.5	13.7	18.6	5.3	8.9	9.1	25.4
Petersburg	1.8	-11.5	324.2	N.A.	-6.3	19.6	-1.7	-6.7	2.5	17.6
Richmond	10.2	4.4	13.8	14.8	15.1	27.5	2.2	2.8	6.3	24.6
Roanoke	12.2	9.9	9.6	12.3	12.6	21.6	2.6	3.8	15.0	26.7
Staunton	4.7	27.1	-53.9	N.A.	3.2	26.1	N.A.	N.A.	-2.0	13.2
Williamsburg	6.9	19.4	71.5	8.6	N.A.	17.7	N.A.	9.0	2.1	15.2
Winchester	9.7	14.7	21.4	12.3	13.7	19.3	N.A.	11.8	3.7	37.1

*Computation of City Index is based upon a weighted arithmetic mean of all business and economic components listed except Building Permits and Bank Debits, which are excluded because of their highly erratic nature.
#Virginia Employment Commission data which lag behind current reports.
†Preliminary data based on a survey sample.
‡Revised data based on sales tax information which lags behind current reports.

the same as in June. Some strong upward momentum still exists in that area.

Cape Charles-Exmore, reflecting the Eastern Shore, levelled off in July, except for new car sales. **Charlottesville's** general economic activity was about on par with or somewhat below last July. However, the final report on June taxable sales indicates **some** types of retail businesses must be doing exceptionally well. Both **Danville** and **Franklin** seem to have hit a plateau in July, with building permits down and no upward momentum in evidence.

In **Fredericksburg,** the growth rates slowed down across the board, moving more in line with average State growth rates, with the notable exception of new car registrations, an activity in which they have had a stellar performance all year. **Harrisonburg,** on the other hand, remained generally at the same level of activity as last year, with some growth in retail sales but a lower rate of increase than in June. **Lynchburg** had higher employment growth than the Commonwealth in June, and the July electricity growth at considerably better than the State average implies manufacturing activity continues to increase. Their most impressive gain in July, however, was the high growth in retail sales, principally nondurables and services — their 26.4 percent increase was the highest in the State.

Both portions of the **Norfolk-Virginia Beach-Newport News** Metropolitan Statistical Area continued to show overall steady growth. The Norfolk side had the better performance for our two lagged variables, the June employment and taxable sales growth rates. However, the Newport News side faired somewhat better in the July figures, with continued high growth in building permits and the better growth rate in new car registrations.

In July, Petersburg generally continued the upward momentum which began in June. Building permits were up 560.0 percent, total spending as evidenced by bank debits soared, and new car registration growth was 53.3 percent, the highest in Virginia. The retail sales sample was a soft spot with only 1.0 percent growth in July, but the broader taxable sales measure for June showed a 30.2 percent increase compared to 21.2 percent in May. When the taxable sales figures for July are available, they should reveal overall retail trade grew by substantially more than our July sample indicates. Up the road, **Richmond's** results were less impressive. Retail trade in durable goods did grow strongly, and nondurable sales growth evidently is growing more rapidly also, but in general Richmond's growth still remains somewhat below the average for the State.

Roanoke is continuing to grow strongly in retail trades, both in durable and nondurable goods, with growth rates well above those for Virginia — its growth ranked second in the State for both our retail sales measures. Also, the very high growth in electricity consumed implies manufacturing activity is increasing more rapidly. **Staunton,** on the other hand, still is revealing a rather flat economic situation, below the State average and about equal to or only slightly better than last year in most categories.

In **Williamsburg,** building permits accelerated in July and total spending as indicated by bank debits soared. But, retail trade growth in general was well below the State averages, and our expectations, because tourism declined slightly in July compared to last year. For **Winchester,** the July figures as well as a comparison to last month's results generally show a slowdown in economic activity. The only outstanding growth rate was the reported 47.6 pecent increase in **June's** taxable sales, the month prior to the current slowdown. Hopefully they will regain the momentum they enjoyed earlier in the year.

In sum, the general Virginia performance in July showed the steady or slower growth expected, except for the surge in new car registrations, and our growth was on par with or better than that of the nation. However, the growth rates varied widely from locality to locality, with some areas achieving outstanding growth while some others were just maintaining last July's level of business activity. Not as balanced from area to area as we would like, and as we hope it will become as the nation's recovery becomes more mature.

RLP

The Deficit — A Guide to the Rhetoric

THE DEFICIT — that expression has been front-page news so frequently in the last three years that reporters no longer even define it. They assume everyone knows by now it refers to current Federal budget revenues minus Federal government expenditures. In fact, there are at least three widely used measures of the deficit, so even the historical amounts for prior years are reported differently, depending on which measure the author uses. However, by **any** measure the recent and projected Federal deficits are **huge,** so the definitional issue is quite minor. Our focus this month is to offer some guidelines for intepreting all the rhetoric we are being inundated with this year.

Effects of Deficits. Deficits are like drugs. They can be a boon to society, curing ills and making it healthier; or, they can be harmful, sapping society's strength and creating painful side effects which may last for years. The key is whether the deficits are cyclical or structural.

Cyclical Deficits. A cyclical deficit is one "that occurs because the unemployment rate exceeds the inflation threshold level of unemployment, i.e., the minimum level of employment (6-6.5 percent) that can be sustained without raising the rate of inflation "(**Economic Report of the President, 1984,** p. 35). Such deficits occur largely automatically in a recession and the initial stage of a recovery, when low output and income reduce Federal tax revenues and increase Federal outlays for cyclically sensitive programs such as unemployment benefits and welfare programs. Such cyclical deficits are helpful to society for several reasons. First, they provide help to people severely hurting during the recession and recovery. Secondly, they create demand for goods and services at a time when we have substantial idle capacity, in people and machines, stimulating growth in output that otherwise would not be produced. Equally important, the cyclical deficits usually do not conflict with monetary policy. A monetary policy of "normal" rates of money growth when the economy is operating at below-normal levels generally means sufficient credit will be available to finance the growth of private demand **and** the cyclical deficit without putting strong upward pressure on interest rates.

Example of a Primarily Cyclical Deficit. In fiscal year 1983 the Federal deficit was $195.4 billion, far above any previous deficit. In that recovery year, the total dollar value of our Gross National Product (GNP) grew by 10.4 percent from the fourth quarter of 1982 through the fourth quarter of 1983. That growth rate consisted of a real increase of 6.3 percent, with an inflation rate of only 3.8 percent (down from 4.4 percent in the preceding four quarters and 8.6 percent from 1980:4 through 1981:4). During the same period, real private domestic investment, our major source of new productive capacity for the future, grew by 14.2 percent.

Even with the high demand growth, interest rates for businesses remained stable. Plus the Federal Reserve System was in an environment where it could allow the money supply to grow at a 9.8 percent rate, sufficient to meet the credit demands of consumers, businesses, and government, without igniting the inflationary fuse. The nation benefited strongly from that deficit: high real growth with lower inflation and stable interest rates, lowered Federal taxes yet continued high Federal spending to meet national priorities and social needs. That high deficit also was cited by a large number of forecasters as a primary reason for the abnormally high real growth in the first and second quarters of 1984.

Structural Deficits. "A structural deficit is the amount . . . that would remain even if the unemployment rate were at the inflation threshold level . . . . [estimated by the President's advisors to be] 6.5 percent" (ibid., p. 36). So, this deficit amount still would exist even if the economy were operating at a very high level of employment and capacity utilization. In that environment, the structural deficit generally would have a very unhealthy effect on the U.S. economy. First, government-induced demand would be in direct competition with private demand for the limited real output, driving up the inflation rate. That brings fiscal policy into direct conflict with monetary policy, which would have to be tighter to prevent an accelerating inflationary spiral. Secondly, the need to finance those deficits by borrowing forces the Federal government to outbid private businesses for savings which otherwise would be available to finance private investment in plant and equipment as well as housing. Our private sector productive capacity would grow at a slower rate, reducing the potential long-run growth rate for the nation. The inflation rate and interest rates would be higher, so long as we remained at a high employment level of output. However, these effects of the structural deficit would destabilize the economy and make a recession likely, so the high employment output could not be maintained: the all too familiar and painful "boom and bust" pattern would become a regular phenomenon. It is the prospect of high **future** structural deficits and their consequences, **not** the recent cyclical deficits, which is worrying private economists, the financial markets, and the Federal Reserve System.

Future Structural Deficits. The August 6, 1984 **Economic and Budget Outlook** prepared by the Congressional Budget Office estimated what the structural deficits would be in each of the next five fiscal years, **if** the economy were at 6 percent unemployment. Their estimates include the effects of the recently passed "down payment" on deficit reduction. The estimated structural deficits and their percent of **high-employment** Gross National Product are: Fiscal year 1985 (FY85), $146 billion, 3.6 percent of GNP; FY86, $167 billion, 3.9 percent of GNP; FY87, $195 billion, 4.2 percent of GNP; FY88, $221 billion, 4.4 percent of GNP; and FY89, $246 billion, 4.6 percent of GNP. Thus they expect the structural deficits to increase steadily, not only in dollar amounts but as a percent of the high-employment GNP. President Reagan's August 16 outlook, which assumes higher GNP growth rates in the future than does the CBO outlook, essentially projects an FY88 structural deficit of $159.7 billion and for FY89, $139.3 billion. The President's report does show lower projected deficits; but, it also specifically illustrates and states that growth alone cannot solve this deficit problem. Again, it should be emphasized that both of these sets of estimates are structural deficits, so achieving full employment would **not** reduce them.

Some Aspects of Deficit Remedies. There is no painless method for eliminating the structural deficits, although some methods defer much of the pain until future years. There are basically four options:

1) Pay more taxes, now or later (the longer you wait, the more you would have to pay).
2) Cut Federal expenditure growth, now or later.
3) A combination of more taxes and less expenditure growth.
4) Adopt a **different** tax structure which discourages consumption and encourages saving. With a sufficiently high savings rate, in the near term the nation could finance **both** higher investment to allow high real growth **and** the structural deficits (as Japan, for example, has done for a decade). The higher real growth would have two benefits in the future: the structural deficits would be lower because of more rapidly growing tax revenues; plus, the additional tax revenues required to eliminate these deficits **completely** would be a smaller percent of the higher individual incomes being received.

All of these options mean **consumption** must be lower at some time in the next four years for at least some, if not most, of the U.S. population than it otherwise would have been. With higher tax rates, you will cut consumption. With lower Federal expenditure growth, recipients of Federal payments will have less funds available than presently planned (**not** necessarily lower than presently **received**), forcing their consumption to be less than it would have been. Of course, a combination of these two approaches also lowers consumption, but with different effects on individuals. The fourth option, a **change** in the tax structure towards a consumption-related tax, would encourage a majority of the public to make small reductions in consumption, thus spreading the burden of deficit reduction more broadly across the population. Many see that as the most equitable and least painful approach. That is the reason there is extensive discussion in the press and in Congress about various types of consumption-based taxes. We will discuss some of these various tax proposals in coming months. However, the key point is that **any** fiscal policy proposal which promises to eliminate structural deficits in the future and at least **maintain** our nation's real growth at its historical average of slightly over 3 percent **cannot** by definition succeed unless as a nation we consume a smaller percent of our national income. The question is **who** is being asked (or forced) to consume less, by how much, and when. With those answers, each person must then decide whether the policy being advocated is a just and effective way to move towards our goals as set forth in the Full Employment and Balanced Growth Act of 1978 (popularly known as the Humphrey-Hawkins Bill) of "full employment . . . increased real income, balanced growth, a balanced Federal budget, . . . and reasonable price stability."

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